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THE DECEPTION OF POLITICAL "ARITHMETIC"

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"In political arithmetic, two and two do not always make four." This aphorism is as true today as 200 years ago when first penned by Alexander Hamilton. It may be even more accurate now, since political addition and subtraction often produce results opposite even from the "new math" taught in today's schools.

In the wake of last October's stock market crash, congressional leaders and the Reagan administration negotiated a budget compromise to reassure the world that Washington could manage the nation's fiscal affairs. Congress and the president claimed the pact would "cut" the federal budget deficit by \$76 billion over the next two years, reducing it by \$30 billion in 1988 and \$46 billion in 1989.

Yet, the president's own fiscal year 1989 budget projects a 1988 deficit that is \$3.7 billion lower than 1987's deficit of \$150.4 billion. And, in 1989, the projected deficit is only about \$17 billion lower than in 1988. Old fashioned arithmetic totes up the savings at less than \$21 billion over two years, or \$55 billion less than advertised.

Using Congressional Budget Office figures, the outcome of last year's exercise is even more paradoxical. CBO estimates that the 1989 deficit will equal \$165 billion, or almost \$15 billion more than last year. If CBO is correct, Congress and the president, like Alice, have stepped through the looking glass into Budgetland. There they have found they must raise taxes more and more to keep the deficit from growing—a race we appear to be losing.

How can this be? The key to understanding is to use political arithmetic, a branch of mathematics closely akin to the algebra of the used car lot. As anyone who has attempted to buy a used car knows, we are told we will "save" more by stepping up to

a Cadillac rather than simply replacing our old worn out Chevrolet with a new one. Why? Because as a buyer negotiates, the salesman will "cut" the price of the expensive car more than the cheaper car. The buyer then proudly points to his "savings," masking the higher price he ended up paying. Such a deal!

The bipartisan budget compromise exemplifies the same kind of logic. Rather than comparing this year's and next year's estimated budget deficits, Congress prefers comparing the 1988 deficit to what the 1989 deficit would have been without the budget agreement. So, when it claimed to "cut" the deficit by \$76 billion, Congress really meant that the deficit would be \$76 billion lower than projected estimates before the compromise. So much for the heroic "deficit reduction package." One trembles to imagine the effects of political cowardice if this is heroism.

Practitioners of political arithmetic, such as House Speaker Jim Wright, want us to believe the budget deficit is the fault of the "massive tax cuts" supported by President Reagan. Wright has said we cannot balance the budget if we go on "reducing our revenues by \$135 billion per year." Once the essentials of political arithmetic are understood, it is easy to see through this argument.

While marginal tax rates have been lowered, tax revenues have grown since 1980. After adjustment for inflation, federal receipts have risen by roughly 2.8 percent a year, the same rate as the economy. In 1987, revenues totaled 19.4 percent of GNP, the exact same share of GNP taken in taxes by the federal government in 1980. It would seem that Wright's comment about a loss in revenues is really a complaint that Congress has not allowed taxes to continue growing at the 1980 rate—roughly 17 percent.

Federal spending on the other hand, has almost doubled since 1980, growing from \$591 billion to more than \$1 trillion last year. In inflation-adjusted dollars, real federal spending has increased at an average rate of 3.3 percent a year since 1980. Compare this to a 3.7 percent average annual rate of increase between 1970 and 1980. Congress has not cut spending. It merely has reduced the rate of growth in spending by a paltry 0.4 percent.

The source of the deficit is to be found in the different rates of growth between spending and tax revenues. Since taxes continue to absorb exactly the same share of GNP as they did before the deficit exploded, it should be obvious that the increased rate of federal spending is out of line and is responsible for the deficit. Blaming the deficit on insufficient tax revenues is like accusing the Red Queen of loafing in her race to keep up in Wonderland.

Last year's episode of "Congress In Budgetland" saw taxes raised by \$29 billion over two years. These are real taxes computed by real, not political, arithmetic. Real arithmetic also tells us that in 1989 the deficit will be reduced by \$21 billion from its 1987 level. Old fashioned subtraction reveals that \$8 billion of that tax increase is not

going toward deficit reduction. Put another way, only about 72 cents of every dollar of increased revenues from the budget compromise will go toward deficit reduction.

Where did the other 28 cents go? Think of it as political profit, a 28-cent commission "earned" by Congress on the sale of the bipartisan deficit reduction package to the American public. Of course, the \$8 billion was not divided equally into 535 payments for each member of Congress. That would be old fashioned graft. Instead, the commission was taken in the form of political currency--increased public spending conferred strategically on selected segments of the electorate. And, that currency was calculated to buy votes to help keep each member safely ensconced in office. The overall rate of re-election in the Congress currently stands at about 90 percent.

As the bipartisan budget compromise illustrates, even when a perceived crisis of confidence requires Congress and the president to take dramatic action, Congress still insists on its commission and on spending part of the tax increase. Therefore, it should not be surprising to discover that during more normal times, Congress has been even more profligate. For every \$1.00 increase in receipts between 1980 and 1987, Congress spent \$1.41. (If one accepts CBO estimates, the crisis-induced 1987 budget agreement will produce a rise in spending of \$1.51 for every \$1.00 of additional revenues.) Using this rule of thumb, a tax increase equal in size to the 1989 deficit would lead not to a balanced budget but to a rise in spending of about \$183 billion and an even larger deficit. In the words of the popular country western song, "One step forward and two steps back/Ain't gonna get too far like that."

The solution to balancing the budget is straightforward. It should not involve any kind of tax increase. Freeze aggregate spending for a period of two years and the budget will be balanced. An alternative would be the "Two Percent Solution," a reduction in the growth rate of federal spending just enough to bring it into line with the long run growth rate of the economy and federal tax revenues. By holding the annual increase in federal expenditures to 2 percent, the budget would come into balance in 1994 based upon current Office of Management and Budget estimates.

This is responsible fiscal arithmetic, not the convoluted logic of Congress In Budgetland. Until Congress is willing to put aside political arithmetic in order to solve America's deficit problem, its budgets will continue to rival the nonsense of Lewis Carroll--only without the humor.